TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING #97-16

WARNING

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.

SUBJECT

Whether The Taxpayer's Tennessee activities create sufficient nexus to subject the corporation to Tennessee corporate franchise, excise taxes.

SCOPE

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the Department by the taxpayer. The rulings herein are binding upon the Department, and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the Commissioner at any time. Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

(A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
(B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
(C) The applicable law must not have been changed or amended;
(D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
(E) The taxpayer directly involved must have acted in good faith in relying upon the ruling and a retroactive revocation of the ruling must inure to his detriment.

FACTS

The Taxpayer is a [STATE A - NOT TENNESSEE] "C" corporation conducting business from its home office and warehouse located in [CITY 1], [STATE A - NOT TENNESSEE]. The Taxpayer also has offices and warehouse facilities in [CITY 2], [STATE A - NOT TENNESSEE] and [CITY 3], [STATE B - NOT TENNESSEE]. All inventory is maintained at these sites. The Taxpayer does not maintain office space or inventory in Tennessee. The Taxpayer does not have any other income

producing property including realty, tangible personal property, trademarks, tradenames, franchise rights, computer programs, copyrights, patented processes, or licenses in Tennessee. The Taxpayer is not a party to any corporate partnerships or joint ventures operating in Tennessee.

[PRODUCT] devices are sold by The Taxpayer for [TYPE BUSINESS] use and The Taxpayer also acts as a distributor or manufacturer's representative. Revenue is generated by purchasing and reselling products, selling products drop shipped by manufacturers to the customer's location, and commission income when acting as a manufacturer's representative. Assembly of products is sometimes completed at one of the company's warehouse locations in [STATE A - NOT TENNESSEE] or [STATE B - NOT TENNESSEE]. The Taxpayer states that no services to customers are rendered outside [STATE A - NOT TENNESSEE] or [STATE B - NOT TENNESSEE]. Products are shipped to the customer by outside trucking companies.

None of The Taxpayer's employees reside in Tennessee. Almost all of its sales are solicited by telephone from one of its three office locations in [STATE A - NOT TENNESSEE] and [STATE B - NOT TENNESSEE]. Sometimes sales are solicited by fax request, mail, or occasionally, by direct solicitation at the customer's place of business. Approximately 99% of The Taxpayer's Tennessee sales are made by telephone from the office in [CITY 3], [STATE B - NOT TENNESSEE]. Merchandise is shipped by an outside carrier directly to the customer in Tennessee.

One of The Taxpayer's salespersons from [STATE B - NOT TENNESSEE] will, occasionally, make a sales call in Tennessee. On such occasions, the salesperson may discuss new equipment that may be of interest to the customer. The salesperson may also visit customers in Tennessee to assist them in determining their needs and to determine whether their needs can be met by the purchase of The Taxpayer's equipment. All sales to Tennessee customers are approved in [STATE B - NOT TENNESSEE] and a credit check is done there prior to approval.

The Taxpayer does no installation or repair of equipment sold to Tennessee customers. Installation is handled by the company purchasing the equipment and is generally done by their subcontractors. Repair work is also handled by the customer and, if major repairs are necessary, the equipment is sent back to [STATE B - NOT TENNESSEE] and repaired there. No employees of The Taxpayer service or repair equipment in Tennessee.

Occasionally, a salesperson from [STATE B - NOT TENNESSEE] will visit a Tennessee customer to observe the start-up of the new equipment after it has been installed and to make recommendations before the equipment is started up. No charge is made for these type visits and no business transactions take place during such visits other than recommending ways to improve efficiency. Only one such visit was made to Tennessee in 1996 and it involved large [PRODUCTS] sold to a customer. For the years 1993 through 1995, the taxpayer states that a maximum of three visits of this nature took place each year, although there may have been years in which no such visits occurred.

The Taxpayer states that it files sales and use tax returns in Tennessee.

ISSUE

Do the Tennessee activities described subject The Taxpayer to Tennessee corporate franchise, excise taxes ?

RULING

Present Tennessee activities do not create sufficient nexus to subject The Taxpayer to Tennessee franchise, excise taxes. However, in the event that The Taxpayer's Tennessee activities expand or change in the future, the new facts created by such changes or expansions would have to be evaluated to determine if nexus for Tennessee corporate taxation exists.

ANALYSIS

APPLICABLE STATUTORY AND CASE LAW

T.C.A. Sections 67-4-806(a) and 67-4-903(a) impose Tennessee corporate franchise, excise taxes on "All corporations, . . . organized for profit under the laws of this state or any other state . . . and doing business in Tennessee . . .". Tennessee law does not define the term "doing business in Tennessee", but Title 15 U.S.C.A. § 381(a), better known as Public Law 86-272, prohibits imposition of a net income tax when the taxpayer's only business in the taxing state is solicitation of sales of tangible goods in interstate commerce. The federal statute reads as follows:

> "(a) No State . . shall have power to impose . . . a net income tax on the income derived within such State by any person from interstate commerce if the only business activities within such State by or on behalf of such person during such taxable year are either, or both, of the following:
>
> > (1) the solicitation of orders by such person, or his representative, in such State for sales of tangible personal property, which orders are sent outside the State for approval or rejection, and, if approved, are filled by shipment or delivery from a point outside the State; and
> > (2) the solicitation of or by such person, or his representative, in such State in the name of or for the benefit of a prospective customer of such person, if orders by such customer to such person to enable such customer to fill orders resulting from such solicitation are orders described in paragraph (1)."

The issue in *Wisconsin Department of Revenue v. William Wrigley, Jr. Co.,* 112 S.Ct. 2447 (1992) was the scope of Title 15 U.S.C.A. § 381 and the activities it protects. In *Wrigley,* the U.S. Supreme Court held that "solicitation of orders" protected includes not only any speech or conduct that explicitly or implicitly invites or proposes an order, but also covers those activities that are entirely ancillary to requests for purchases and serve no independent business function apart from their connection to soliciting orders.

Although the entire process associated with the invitation of an order is protected, the phrase "solicitation or orders" does not embrace all activities that are routinely or even closely associated with solicitation or customarily performed by salesmen. *Id.* at 2455 and 2456. Activities that a company would have reason to engage in anyway, apart from solicitation or orders, but chooses to allocate to its in-state sales force are not protected from state corporate taxation by federal law. *Id.* at 2456.

For example, providing a car and a stock of free samples to salesmen is part of the "solicitation of orders" because the only reason to do it is to facilitate requests for purchases. However, employing salesmen to repair or service the company's products is not part of the "solicitation of orders" since there is good reason to get that done whether or not the company has a sales force. Some activities, such as repair and servicing of products after they are sold to the customer, may indirectly help increase future purchases, but such activities are not ancillary to requesting purchases and cannot be converted into "solicitation" by merely being assigned to a salesman. Even if engaged in exclusively to facilitate requests for purchases, the maintenance of an office within the state by a company, or on its behalf, goes beyond the "solicitation of orders" and will subject the company to taxation in the state where the office is maintained. Activities that take place after a sale will ordinarily not be entirely ancillary to requests for purchases, but there may be exceptions. *Id.* at 2457.

However, under the old and well established maxim *de minimis curat lex* ("the law cares not for trifles"), the *Wrigley* court held there is a *de minimis* principle applicable in construing Title 15 U.S.C.A. § 381. A corporation may engage in certain *de minimis* activities without incurring corporate tax liability even though such activities, were they not *de minimis,* would ordinarily create sufficient nexus to impose the tax. Whether an in-state activity, other than solicitation of orders, is sufficiently *de minimis* to avoid loss of tax immunity conferred by Title 15 U.S.C.A. § 381 depends upon whether the activity establishes a nontrivial additional connection with the taxing state. *Id.* at 2458.

APPLICATION OF STATUTORY AND CASE LAW TO FACTS PRESENTED

In order to determine whether The Taxpayer is "doing business in Tennessee" so as to be subject to corporate franchise, excise taxes, we must carefully examine each of its activities in Tennessee in the light of the immunity provisions set forth in Title 15 U.S.C.A. § 381 and the criteria set fourth by the U.S. Supreme Court in *Wrigley.*

Title 15, U.S.C.A. § 381(a)(1) prohibits the imposition of a state income tax when the only activity in the state is solicitation of orders for sale of tangible personal property when such orders are sent outside the state for approval or rejection and approved orders are shipped and delivered from a point outside Tennessee.

The Taxpayer does not maintain an office in Tennessee. No inventory or other income producing property of a real, tangible or intangible nature is maintained by The Taxpayer in Tennessee. The Taxpayer does no installation or repair work in Tennessee. Assembly of products is done at one of the Taxpayer's warehouses in [STATE A - NOT TENNESSEE] or [STATE B - NOT

TENNESSEE]. None of these activities or maintaining of property takes place in Tennessee, and thus they do not subject The Taxpayer to Tennessee corporate franchise, excise taxes.

Almost all (99%) of The Taxpayer's sales to Tennessee customers are made by telephone from [STATE B - NOT TENNESSEE] and are shipped by an outside carrier directly to the customer in Tennessee. On occasion, sales may be solicited from [STATE B - NOT TENNESSEE] by fax or by mail. These sales to Tennessee customers are made without the taxpayer ever leaving [STATE B - NOT TENNESSEE] and do not subject The Taxpayer to our franchise, excise taxes.

Occasionally, The Taxpayer solicits purchases from Tennessee customers by sending a salesman into Tennessee. On such occasions, the salesperson may discuss new equipment that may be of interest to the customer. The salesperson may also visit customers in Tennessee to assist them in determining their needs and to determine whether their needs can be met by the purchase of The Taxpayer's equipment. All sales to Tennessee customers are approved in [STATE B - NOT TENNESSEE] and a credit check is done there prior to approval. These activities in Tennessee serve no independent business function apart from solicitation of orders. There would be no reason to engage in such activities in Tennessee were it not for the hope that purchases will result. These sales are protected by Title 15, U.S.C.A. § 381(a) and do not subject The Taxpayer to Tennessee franchise, excise taxes.

The only remaining activity The Taxpayer has in Tennessee is visits by salespersons to observe the startup of new equipment and make recommendations for improvement of efficiency. No charge is made for this service. The *Wrigley* Court observed that activities that take place after a sale will ordinarily not be entirely ancillary to requests for purchases. *Id.* at 2457. Since these visits take place after the sale has already been made, their purpose can not possibly be to solicit orders. While it may be desirable for The Taxpayer to send a salesperson into Tennessee to observe the startup of new equipment and give the customer advice on how to improve its efficiency, and while such visits may indirectly help increase purchases, they are not ancillary to requesting purchases and, therefore, would ordinarily create sufficient nexus in Tennessee to subject The Taxpayer to franchise, excise taxes. An activity may indirectly help increase purchases and yet not be ancillary to requesting purchases. *Id.* at 2457. Activities that a company would have reason to engage in anyway, apart from solicitation of orders, are not protected from state corporate taxation just because they have been allocated to a salesperson. *Id.* at 2455 and 2456.

However, under the facts given, visits by The Taxpayer's salespersons to observe the startup of new equipment and make recommendations for improvement of efficiency occur only occasionally. The Taxpayer states that only one of these visits was made in Tennessee in 1996 and that for the three years prior to 1996, a maximum of three of these type visits per year were made. Visits of this nature that occur only occasionally and infrequently would fall within the *de minimis* exception of *Wrigley* and would not operate to destroy The Taxpayer's Tennessee franchise, excise tax immunity under Title 15 U.S.C.A. § 381.

Certainly, the one visit of this type in 1996 and the maximum of three visits per year for the three years prior to 1996 would fall within the *de minimis* exception. However, at some point these type visits to Tennessee customers could reach a volume and frequency that would remove them from the *Wrigley de minimis* exception. At that point, The Taxpayer would be subject to Tennessee franchise, excise taxes.

CONCLUSION

None of The Taxpayer's present Tennessee activities create sufficient nexus in Tennessee to subject it to the Tennessee corporate franchise, excise taxes. Should the corporation's Tennessee activities expand or change in the future, the new facts created by such changes or expansions would have to be evaluated to determine if nexus for Tennessee corporate taxation exists.

_____
Arnold B. Clapp, Senior Tax Counsel

APPROVED: _____
Ruth E. Johnson, Commissioner

DATE: 6-2-97